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No. 08-1409

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

FORD MOTOR COMPANY,
Petitioner,

v.

DELAWARE DIRECTOR OF REVENUE,
Respondent.

On Petition for Writ of Certiorari to the Supreme Court of Delaware

BRIEF OF *AMICI CURIAE* COUNCIL ON STATE TAXATION AND NATIONAL ASSOCIATION OF MANUFACTURERS IN SUPPORT OF PETITIONER

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INTEREST OF *AMICI CURIAE*

This brief *amici curiae* in support of Petitioner ("Ford") is filed on behalf of the Council On State Taxation ("COST") and the National Association of Manufacturers ("NAM").

COST is a non-profit trade association formed in 1969 to promote equitable and nondiscriminatory state and local taxation of multi-jurisdictional business entities. COST represents nearly 600 of the largest multistate businesses in the United States; companies from every industry doing business in every state.

The NAM is the nation's largest industrial trade association, representing small and large manufacturers in every industrial sector and in all 50 states. The NAM's mission is to enhance the competitiveness of manufacturers by shaping a legislative and regulatory environment conducive to U.S. economic growth and to increase understanding among policymakers, the media, and the public about the vital role of manufacturing to America's economic future and living standards.

Amici's members' interest in this case is both specific and general. Many *amici* members conduct business in Delaware and pay taxes in the jurisdiction. The decision of the Delaware Supreme Court that an unapportioned gross receipts tax is constitutional raises a risk that Delaware or its localities may each attempt to allocate other types of receipts entirely to their taxing jurisdiction. Such an unconstitutional extension of the State's taxing jurisdiction threatens the fragile balance of many of *amici*'s members' tax liability in multiple states.

On a broader level, the decision adversely affects all *amici* members because unapportioned, unconstitutional local taxes continue to be a problem in other jurisdictions. *Amici* have witnessed a tremendous growth in the application of gross receipts taxes. Gross receipts taxes that are neither apportioned nor fairly apportioned by a state or local taxing jurisdiction can lead to unjust results. Thus, *amici*'s members have a strong interest in the Court mandating that state and local governments fairly apportion gross receipts taxes imposed on the privilege of doing business. Without the Court's guidance, businesses will be subject to an increasing number of unapportioned business taxes, resulting in

multiple taxes with a potential multiplier as high as the number of jurisdictions in which a business is subject to tax. By granting the Petition for Certiorari, this Court can clarify the extent that state and local governments can impose their business activity taxes.

STATEMENT OF THE CASE

The state of Delaware imposes business activity taxes, including a gross receipts tax. Among the activities subject to the gross receipts tax is the wholesaling of goods. The tax on wholesaling is measured by the entire gross receipts received from wholesale sales of goods delivered to locations in the State, regardless of where the actual sales, including title transfer, occur.

Ford's wholesaling activities that ultimately result in the receipt of a vehicle by a Delaware dealer include a multi-step order process, most of which occurs outside the State of Delaware. Ford challenged the validity of the tax, including a Commerce Clause claim that the State's gross receipts tax unduly burdens interstate commerce by failing to fairly apportion the tax to Ford's activities conducted within the State. Finding that the risk of double taxation was a minor constitutional concern, the Delaware Supreme Court ultimately rejected Ford's Commerce Clause claim.

SUMMARY OF ARGUMENT

The Court should grant review in this case because the rule for determining whether a gross receipts tax must be apportioned has created great confusion in state courts-confusion only this Court can resolve. The Delaware Supreme Court's holding that the Commerce Clause does not bar a state from imposing

a gross receipts tax on 100 percent of a taxpayer's gross receipts derived from interstate activities—the vast majority of those activities occurring outside of the State—is but one example of the continued confusion.

As acknowledged by this Court in *Oklahoma Tax Commission v. Jefferson Lines, Inc.*, 514 U.S. 175 (1995), a gross receipts tax that is akin to an income tax is required to be apportioned to reflect the location of the various interstate activities by which it was earned. Conversely, sales taxes need not be apportioned provided they satisfy all other requirements articulated in *Jefferson Lines*. A great deal of confusion continues to surround the application of this distinction to gross receipts taxes-are they more akin to an income tax or a sales tax?

The conflict over whether the imposition of a business activity tax on a taxpayer's unapportioned gross receipts is fairly apportioned is not an issue limited only to Delaware. States and cities across the United States have increasingly adopted alternative tax regimes that differ greatly from traditional income taxes, and State courts around the country are divided on how to properly apportion such taxes. A denial of *certiorari* in this case will only allow the problem to persist and will perpetuate confusion and uncertainty with governmental tax policy makers and the taxpaying business community.

Lastly, in such tough economic times, businesses and States need clear direction from this Court. States facing overwhelming revenue shortfalls must reliably know what business income they may constitutionally tax. Businesses such as Ford, which timely file and pay tax due, should not be subject to double taxation on gross receipts that the Commerce

Clause demands be fairly apportioned. It is time for this Court to provide guidance on this increasingly prevalent issue.

ARGUMENT

I. THIS COURT SHOULD OFFER GUIDANCE ON WHETHER APPORTIONMENT IS REQUIRED FOR GROSS RECEIPTS TAXES THAT ARE NOT TRANSACTIONAL IN NATURE UNDER *JEFFERSON LINES*

The key issue in need of resolution in this case is the application of this Court's clear requirement that income taxes be fairly apportioned. States and localities have repeatedly argued that gross receipts taxes are more akin to sales taxes that need not be apportioned.

In 1977, the Supreme Court adopted a four-part test for determining whether a state or local tax on an interstate business is valid under the Commerce Clause. *Complete Auto Transit Inc. v. Brady*, 430 U.S. 274 (1977). In *Complete Auto*, the Court held that a tax is permissible under the Commerce Clause only when the tax is "applied to an activity with a substantial nexus with the taxing state, is fairly apportioned, does not discriminate against interstate commerce, and is fairly related to the services provided by the State." *Id.* at 279. It is the second requirement—fair apportionment—that is at issue in this case.

The Supreme Court subsequently further refined the fair apportionment prong of the Commerce Clause analysis. To be fairly apportioned, a tax must be both internally and externally consistent. *Goldberg v. Sweet*, 488 U.S. 252 (1989).

Even before the Court consolidated its disparate Commerce Clause tests in *Complete Auto* and *Goldberg v. Sweet*, the Court was confronted with the question of the constitutionality under a fair apportionment analysis of a tax on the unapportioned gross receipts of a business earning those receipts in multiple jurisdictions. In *Central Greyhound Lines v. Mealey*, 334 U.S. 653 (1948), the State of New York sought to impose an unapportioned gross receipts tax on all the taxpayer's nationwide gross receipts from transportation services, even though 43% of the transportation (measured by mileage) actually took place in New Jersey and Pennsylvania. The Supreme Court held that the tax violated the Commerce Clause because it was not apportioned:

> New York claims the right to tax the gross receipts from transportation which traverses New Jersey and Pennsylvania as well as New York. To say that this commerce is confined to New York is to indulge in pure fiction. To do so, does not eliminate the relation of Pennsylvania and New Jersey to the transactions nor eliminate the benefits which those two States confer upon the portions of the transportation within their borders. Neither their interests nor their responsibilities are evaporated by the verbal device of attributing the entire transportation to New York.

Central Greyhound, 334 U.S. at 660.

Central Greyhound predates the now-classic four-part Commerce Clause test of *Complete Auto* discussed above, under which all state and local taxes are tested. However, *Central Greyhound* remains a pertinent precedent for purposes of testing gross receipts taxes, as can be seen from this Court's decision

in *Oklahoma Tax Commission v. Jefferson Lines, Inc.*, 514 U.S. 175 (1995). There, the Court distinguished the apportionment analysis of a tax on a distinct transaction (such as a sales tax) from a tax on the income from business activity (such as the gross receipts tax imposed by Delaware in this case).

A state imposing a gross receipts tax in the form of a sales tax does not necessitate the same apportionment requirements because the manner in which the tax is imposed and any allowable credits prevents a concern with double taxation. In acknowledging *Central Greyhound* covered the same type of bus services provided by *Jefferson Lines*, the Court in *Jefferson Lines* noted:

> Here, in contrast, the tax falls on the buyer of the services, who is no more subject to double taxation on the sale of these services than the buyer of goods would be. The taxable event comprises agreement, payment, and delivery of some of the services in the taxing State; no other State can claim to be the site of the same combination.

Jefferson Lines at 190. *See also Western Live Stock v. Bureau of Revenue*, 303 U.S. 250 (1938) where the Court looked at New Mexico's gross receipts tax (akin to a sales tax) and stated, "The tax is not one which in form or substance can be repeated by other states in such manner as to lay an added burden on the interstate distribution of the magazine." *Id.* at 260.

The tax imposed by Delaware, however, is not akin to a sales tax. The State's gross receipts tax is far more analogous to a net income tax, because it taxes the aggregate of all sales in the taxing state at once. Similar to *Central Greyhound*, the gross receipts tax imposed by Delaware is "simply a variety of tax on

income, which was required to be apportioned to reflect the location of the various interstate activities by which it was earned." *Jefferson Lines* at 190. The Delaware Supreme Court in its decision below acknowledged in its decision that a State may tax "only that portion of the revenues from interstate activity which reasonably reflect the in-state component of the activity being taxed." *Ford Motor Co. v. Director of Rev.* 963 A.2d 115, 122 (Del. 2008) (citing *Goldberg*, 488 U.S. at 262). However, that court mistakenly upheld the application of the gross receipts tax on 100% of the sales that were physically delivered in Delaware, without providing any credit for the income-producing activities that occurred well before the automobiles crossed the state line.

The Supreme Court of Delaware's analysis is too expedient. It fails to take into account that *Jefferson Lines* reaffirmed the Court's holding in *Central Greyhound* that a gross receipts tax that operates as a variety of an income tax must be apportioned among the jurisdictions in which the activities generating the receipts are performed. Following the *Jefferson Lines* decision, three preeminent state tax scholars and academicians examined the distinction between sales and gross receipts taxes for Commerce Clause purposes, in light of *Jefferson Lines*:

> In distinguishing those levies whose tax base must be divided among the states in order to satisfy the Commerce Clause's fair apportionment requirement from those levies whose tax base may be taxed in full by a single state without offending the Commerce Clause, the Court in *Jefferson Lines* drew a line in the sand between 'sales taxes' and 'gross receipts taxes.' The Court treated the former as a levy on a 'taxable event'

> that occurred, or was deemed to occur, wholly within the state, thereby making apportionment of the base unnecessary. *The Court treated the latter as 'simply a variety of a tax on income, which was required to be apportioned to reflect the location of the various interstate activities by which it was earned.'*

W. Hellerstein, M. McIntyre, R. Pomp, "Commerce Clause Restraints on State Taxation After *Jefferson Lines*," 51 Tax L. Rev. 47, 86 (1995). Thus, *Central Greyhound*, as affirmed in *Jefferson Lines*, requires the apportionment of a gross receipts tax among the jurisdictions in which the activities generating the receipts are performed.

In summary, *Jefferson Lines* teaches us a gross receipts tax not operating like a sales tax must be apportioned; *Complete Auto* teaches us that a tax must be fairly apportioned; *Goldberg v. Sweet* teaches us that to be fairly apportioned, a tax must be imposed only on the "portion of the revenues from the interstate activity which reasonably reflects the instate component of the activity being taxed"; and *Central Greyhound* teaches us that for a gross receipts tax to reasonably reflect the instate component of the activity being taxed, it must be apportioned among all of the jurisdictions in which the activity giving rise to the tax is performed. Thus, under *Jefferson Lines*, *Complete Auto* and *Central Greyhound*, Delaware's tax on gross receipts must be apportioned, and under *Goldberg v. Sweet*, the apportionment method must account for all of the jurisdictions in which the activity generating the taxed receipts occurs. Hence, the relevant inquiries are: "what is the activity being taxed?" and "where is that activity carried on?"

The Petitioner in this case is being taxed on its activity of wholesaling motor vehicles. The logical next step in the constitutional analysis under *Goldberg v. Sweet* is to locate where that activity is performed. Delaware's position places 100% of the activity in the State while the Petitioner's position would place something less in the State. Thus, the location of the activity being taxed (wholesaling vehicles) is both within and without the State-with much more of the activities to make the sale occurring outside of and not within the State.[1]

Thus, since Delaware taxes 100% of the receipts but only a portion of those receipts are attributable to Delaware, the State is taxing more than the activity which reasonably reflects the instate component of the activity being taxed. Because the State is taxing more than its reasonable share of the activity, its application of its gross receipts tax to 100% of Ford's wholesale receipts is unconstitutional.

II. THE APPORTIONMENT OF BUSINESS ACTIVITY TAXES IS A PERSISTENT AND WIDESPREAD PROBLEM IN NEED OF CLARIFICATION BY THIS COURT

Amici are gravely concerned with the recent growth in the imposition of taxes on unapportioned, interstate gross receipts. With nearly 1,200 separate state and local business activity taxes collected by state and local governments, such taxes have increasingly become the subject of litigation around the

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[1] The Petitioner and Respondent entered into an extensive stipulation of the facts, which found that the "wholesaling process" does not occur only in one State, but occurs in a number of States and eventually leads to the delivery of a wholesale vehicle to an independent dealership in Delaware.

country and will continue to do so unless this Court gives clear guidance. As evidenced in Petitioner's brief, courts around the country are divided on whether the Commerce Clause requires apportionment of gross receipts taxes derived from multistate activity. *Amici* submit this brief to bring to the Court's attention just how varied the rulings on the apportionment of business activity taxes are and how significant the issue is to multijurisdictional taxpayers.

A. The Issue of Unapportioned Gross Receipts Taxes is a Real and Emergent Issue

The number of states and localities that impose business activity taxes based upon unapportioned gross receipts is significant. As noted in Petitioner's brief, the types of these taxes range from newly enacted state-level taxes[2] to a plethora of existing local business activity taxes.

An example of a typical business activity tax based upon gross receipts can be found in Kansas City, Missouri. Kansas City, like many Missouri municipalities, imposes business license taxes on individuals and companies for the privilege of doing business in Kansas City. Kansas City, Mo. Ordinance § 40-61 (1967). The tax is imposed at different rates on different business activities, but in many instances, the tax is imposed based upon a percentage of "gross receipts" from business done in Kansas City. Kansas City, Mo. Ordinance § 40-63 (1967). The Kansas City

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[2] Three states have recently imposed gross receipts taxes: The Ohio Commercial Activities Tax (H.B. 66 2005), The Texas MarginTax (H.B. 3 2005), and the Michigan Business Tax (S.B. 94 2007).

ordinance does not allow the tax to be apportioned to account for any portion of business activity that occurs outside of the city. *Id.*

Bristol, Tennessee offers another example of an ordinance imposing a tax on unapportioned gross receipts. Bristol, like many Tennessee cities, imposes an annual tax on the privilege of doing business within the city. Bristol, Tenn. Ordinance § 66-28 (1980). The tax is based upon a Tennessee statute allowing for the imposition of municipal taxes on the "gross income" of companies doing business in Tennessee cities. Tenn. Code Ann. § 67-4-701, *et seq.* (2007). Like the Kansas City tax, the Bristol tax is not apportioned to account for business activity occurring outside of the city.

Kansas City and Bristol offer but two examples of the 1,200 other taxes imposed on gross receipts. Like Kansas City and Bristol, many of the gross receipts taxes do not allow for the apportionment of receipts where some activity occurs outside of the locality. As demonstrated below, the requirement that these taxes be apportioned has led to litigation in many states to determine whether the lack of apportionment violates the Commerce Clause.

B. Some State Courts Have Held that the Commerce Clause Requires Apportionment of Business Activity Taxes.

When confronted with the issue of fair apportionment of a business activity tax, some state courts have ruled in favor of apportionment, taking the position that to do otherwise would be a Commerce Clause violation. For example, Pennsylvania courts have heard several cases on this issue and generally

rule for an apportionment requirement. In Pennsylvania's seminal case on this issue, *Philadelphia Eagles Football Club, Inc. v. City of Philadelphia*, 823 A.2d 108 (Pa. 2003) the City of Philadelphia attempted to impose a business activity tax on 100 percent of the taxpayer's media receipts although one-half of the games were telecast from venues outside of the city. The Supreme Court of Pennsylvania held that the City of Philadelphia could only impose a business activity tax on revenue generated from games played and broadcast from within Philadelphia, and not media receipts generated from away games. *Id.* at 135. Because the City attempted to apply the tax to all of the receipts, the business activity tax, as applied, violated the Commerce Clause because it failed the external consistency prong of the fair apportionment test. *Id.* at 135.

In *Northwood Construction Co. v. Township of Upper Moreland*, 856 A.2d 789 (Pa. 2004) the Pennsylvania Supreme Court reached a similar result when it held that a business activity tax imposed on 100 percent of a taxpayer's gross receipts from in-state and out-of-state activity violated the Commerce Clause because the vast majority of the company's business took place out-of-state. *Id.* at 799. In *Northwood Construction*, the taxpayer maintained its principal place of business in the Township of Upper Moreland, yet its primary business activities were conducted throughout Pennsylvania, as well as in three other states. The Township attempted to impose its business activity tax on all of the taxpayer's out-of-state receipts. Utilizing this Court's tests in *Complete Auto* and *Goldberg*, the court ruled that although a taxing jurisdiction may impose a business activity tax on receipts from out-of-state work where the taxpayer maintains a base of operations within the municipal-

ity, such treatment is unconstitutional where most of the taxpayer's business activity is conducted outside of the state. *Id.* at 799.

California courts have also discussed this issue. In *City of Los Angeles v. Shell Oil Co.*, 480 P.2d 953 (Ca. 1971) the Supreme Court of California held that only gross receipts directly attributable to selling activities carried on in the City were taxable. In holding that the application of a business activity tax exceeds the City's constitutional powers, the Supreme Court of California stated that the City "refuses to take cognizance of . . . [substantial] out-of-city elements in the measure of its tax—and accordingly purports to tax the total gross receipts derived from the sales in question—solely because the goods are shipped from the City. Such an application . . . is violative of . . . constitutional principles." *Id.* at 966. *See also General Motors Corporation v. City of Los Angeles*, 486 P.2d 163, 173 (Ca. 1971) (stating that the inclusion of unapportioned gross receipts within the tax base results in the taxation of significant extraterritorial values where substantial elements of the sale process which produces such receipts takes place outside the City); *Volkswagen Pacific, Inc. v. City of Los Angeles*, 496 P.2d 1237, 1245 (Cal. 1972) (Court barred assessment of business activity taxes where the city did not apportion the tax to account for selling activity outside the city limits).

Missouri courts have also held that the application of a business activity tax to unapportioned gross receipts is unconstitutional. In *General Motors Corp. v. City of Kansas City*, 1993 Mo. App. LEXIS 1985 (Mo. Ct. App. 1993), the taxpayer operated an automobile assembly facility in Kansas City. Despite the fact that the greatest percentage of the parts

used to assemble the automobiles were manufactured outside of Kansas City, the City attempted to assess its business activity tax upon the total value of cars manufactured in Kansas City. The Court of Appeals of Missouri, Western District, held that the city's business activity tax, as applied, was unconstitutional because the tax was not limited in its application to manufacturing that occurred within the city. *Id.* at 26. A similar result was reached in a more recent Missouri case, *Ford Motor Co. v. City of Hazelwood*, No. 02CC-002296 Slip Op. (St. Louis County Cir. Ct., Mo. 2003), where the St. Louis County Circuit Court held that a business activity tax imposed upon unapportioned gross receipts from vehicles assembled in the city of St. Louis was unconstitutional as applied. *Id.* At 9-13.

In *City of Winchester v. American Woodmark Corp.*, 471 S.E.2d 495 (Va. 1996), the Supreme Court of Virginia struck down the application of a business activity tax to unapportioned revenues as unconstitutional. There, the taxpayer maintained its corporate headquarters in Winchester, but operated 24 facilities in 13 different states-none of which were located in the city. Winchester attempted to impose its business activity tax on 100 percent of the taxpayer's gross receipts, arguing that since the taxpayer is a highly centralized, unitary business all of its gross receipts were in some way attributable to the headquarters office. The Supreme Court of Virginia rejected this argument stating that the imposition of the tax was invalid because it was not apportioned as required by the Commerce Clause. The court reasoned that given the number of facilities and operations outside of the taxing jurisdiction, the value added by the taxpayer's operations within the City

could not possibly produce 100 percent of the revenues. *Id.* at 498.

In *KMS Financial Services, Inc. v. City of Seattle*, 146 P.3d 1195 (Wash. Ct. App. 2006), the Court of Appeals of Washington took the position that "seeking to tax income generated by extraterritorial activities . . . exceeds federal and state constitutional limits." *Id.* at 1198. In *KMS*, the taxpayer was a Washington corporation based solely in Seattle. The taxpayer had nearly 300 registered representatives who worked from 210 business locations in nine western states, including Washington. The City of Seattle imposed its business activity tax on all commissions received at the taxpayer's Seattle office regardless of where the registered representative who generated the commission was based. The Court of Appeals of Washington held that attributing the entire proceeds of taxpayer's registered agent to the city merely because that was the taxpayer's sole office violated the external consistency requirement of fair apportionment, and thus violated the Commerce Clause. *Id.* at 1206.

In addition to the aforementioned cases, other state court decisions have sided with the position that federal Commerce Clause jurisprudence requires the apportionment of multistate gross receipts used to determine a taxpayer's liability for a business activity tax. *See, e.g. Southern Pacific Transp. Co. v. Arizona*, 44 P.3d 1006, 1013, 1017 (Ariz. App. 2002) (stating that a business activity tax on an interstate transaction "will violate the Commerce Clause in the absence of fair apportionment" and holding that a business activity tax could not be constitutionally applied to a taxpayer's railroad gross receipts from transporting goods between the taxing jurisdiction and other

points in the state where a portion of the journey occurred in another state); *Northwest Energetic Services, LLC v. Franchise Tax Bd.*, 159 Cal. App. 4th 841 (Cal. Ct. App. 2008) (holding that a business activity tax was required to be fairly apportioned); *General Motors Corp. v. City and County of Denver*, 990 P.2d 59, 71 (Colo. 1999) (acknowledging that a business activity tax must be fairly apportioned and "may only be imposed on interstate activity that 'reasonably reflects the in-state component of the activity being taxed'" (citing *Goldberg v. Sweet*, 488 U.S. 252, 262 (1989))); *Trinova Corp. v. Michigan Dep't of Treasury*, 498 U.S. 358 (1991) (where an assessment under Michigan's business activity tax, which is levied based upon a three-factor apportionment formula, was at issue).

C. Other State Courts Have Held that the Commerce Clause Does Not Require Apportionment of Business Activity Taxes.

Some state courts have interpreted the Commerce Clause as not requiring the apportionment of business activity taxes. A Delaware Superior Court upheld the imposition of a business activity tax on unapportioned gross receipts based upon the magnitude of the taxpayer's operations in the state. In *Saudi Refining, Inc. v. Director of Revenue*, 715 A.2d 89 (Del. Super. 1998), the taxpayer was a Delaware corporation with its principal place of business in another state. Despite the fact that the only sales the taxpayer made in Delaware were to a single Delaware corporation, the state imposed its business activity tax on the taxpayer's gross receipts attributable to sales of tangible personal property physically delivered in Delaware. The court found

that the magnitude of the goods purchased and the length of time the goods were within the state created sufficient nexus to bring the taxpayer within the purview of the tax. *Id.* at 92.

Further, other state courts have taken the position that the Commerce Clause does not require the apportionment of a business activity tax imposed on gross receipts derived from activity within and without the taxing jurisdiction. *See e.g. Ramsay Travel, Inc. v. Kondo*, 495 P.2d 1172, 1176 (Haw. 1972) (stating that a tax on 100 percent of commission income received by taxpayer from sales derived within and without the state did not contravene the Commerce Clause); *Ford Motor Co. v. City of Seattle*, 156 P.3d 185 (Wash. 2007) *cert denied* 128 S. Ct. 1224 (2008) (holding that a local business activity tax could be imposed on wholesale activity that occurred partially outside of the locality). These decisions are counter to the clear weight of authority and should not be allowed to stand.

CONCLUSION

In conclusion, the State's imposition of its Business Privilege Tax on 100 percent of Ford's wholesaling receipts is unconstitutional because the receipts arose from activities both within and without the state of Delaware. *Amici* respectfully requests this Court to accept the taxpayer's Petition to clarify this issue of national importance.

Respectfully submitted.

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